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Audit's® MARKET ANALYSIS OF SECURITIES OF REITS AND REAL ESTATE COMPANIES

Realty Stock Review

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MARKET STRATEGY: IF VISIBLE DISTRESS IS ALL AROUND, CAN RECOVERY BE FAR AWAY?

Last week in Columbus, O. your editor watched a bulldozer clean up the last rubble from a demolished five-story motel. Built in the mid-1970s with a loan from a mortgage REIT of that day, the motel was foreclosed but was never occupied despite years of sales efforts. The location was just a bit far out and, finally, bulldozing was the only choice.

The motel's demise is a signal to investors that mid-1970s-style property problems are again working thru the system -- mainly for stocks with Southwestern exposure. And that presents investors with opportunities at two different levels. Already action is being seen at both levels:

1. **Stock level.** The bulldozed motel reminds investors that problem properties can hang around to hurt operations for a long time, especially when properties aren't prime in location or design. Hence we don't advise rushing into visibly troubled situations until the smoke clears. Problem properties are now really clobbering some Southwestern realty stocks, and the situation is now so fluid for these companies that we'd avoid their stocks for now. Items:

o **Southland Financial** ($5.25--SFIN--OTC) agreed to sell its downtown Dallas Southland Center and adjoining Sheraton Hotel for a loss from its $126.8 mil. depreciated cost; the complex carried $78.7 mil. debt, leaving $48.1 mil. net equity for SFIN. Sale price and terms weren't given but SFIN said it would report $50 mil. after-tax charge, most relating to the Center and for other losses at its Las Colinas office holdings. Center occupancy fell to 55% when Southland Life moved. SFIN said it defaulted on some debt as part of restructuring efforts (REVIEW, July 24) and may default on more debt. In Las Colinas, SFIN leased 1.2 mil. sq. ft. office space in the first 6 mon., more than all the rest of Dallas.

o **Southwest Realty Ltd.** ($3.63--SWL--ASE) of Dallas put apartment projects in Houston and San Antonio into Chapter XI bankruptcy protection and stopped paying debt service on three additional apartments. SWL has been seeking to restructure $49.9 mil. mortgage debt. SWL lost 41¢ and 67¢ per unit in the June qtr. and six mon. SWL said it's possible but not likely it may also have to seek Ch. XI protection.

o Shares of **California REIT** ($6.00--CT--NYSE) and **CleveTrust Realty Investors** ($9.25--CTRIS--OTC) have been at or near new lows recently, reflecting impact of depressed Southwestern property

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markets. CTRIS became mortgagee in possession of a 187,000 sq. ft. Dallas retail/office complex, whose problems caused a dividend cut. CT also cut its dividend in January because of ills at Dallas apartment/commercial properties.

2. **Takeover level.** When stock prices get kicked around by bum properties, you can generally expect the depressed prices to attract takeover investors. These takeover tries can or cannot be good for investors, depending upon circumstances. They are worth watching mainly for trading opportunities. Current situations:

o **Del E. Webb Corp.** ($25.00--WBB--NYSE) has attracted two investor groups: Industrial Equity (Pacific) Ltd. with a 9.3% stake, and Los Angeles based Hecco Ventures with 9.15%. Events have moved swiftly at WBB: Its June qtr. profit was due almost solely to tax-motivated transactions with native Indian tribes and masked growing deficits in its gambling operations; it announced plans to restructure, perhaps by splitting into two companies. The two suitors then appeared. Industrial Equity, vehicle of New Zealander Ron Brierley, says it wants to buy 50% of WBB. Hecco's managing partner is James J. Cotter, executive vice president of Decurion Corp., parent of Pacific Theaters Corp.

o **Fairfield Communities Inc.** ($9.-88--FCI--NYSE) said Nutrition World, Inc. of Des Plaines, Ill. has bought 9.7% of shares and will seek board representation and propose a merger or other business combination. Nutrition World retails health foods. Little Rock based FCI is a recreational community developer which has sustained losses recently. However FCI earned 13¢ in the June Q; land and commercial sales rose.

o **Consolidated Capital Income Trust** ($10.88--CCITS--OTC) beat a proxy contest by Industrial Equity (see Del Webb, above), then agreed to buy 1.27 mil. shs. back from IEP for $11.50 per sh.; in addition a subsidiary of Johnstown American Cos., the adviser, agreed to pay IEP $1.80 per sh. to prevent IEP from buying shares in JAC or CCITs.

o **National Capital Real Estate Trust** ($2.25--NCETS--OTC) has agreed to restructure as a Delaware corporation in a deal adding $5 mil. new equity investment. Under the plan, two New York City investors, Resource Holdings Equity Corp. and Quest Investors L.P. would buy 1.786 mil. shs. and 2.21 mil. wts. in a new company which would <u>not</u> operate as a REIT. NCETS holders would exchange their 3.645 mil. shs. one-for-one into the new company. New investors would own 33% initially and 52% fully diluted of the new entity. Holders must approve.

These two trends are likely to bring choppy markets in many realty stocks and our advice is to stay a bit looser and willing to take advantage of opportunities that may arise.

RANKING REVIEWS: THREE DIVERSE BUILDERS AND OWNERS SLOW GROWTH BUT HOLD RANKS

This trio offers investors diverse choices in product and location: a seasoned Southeastern suburban office park developer, a major Florida landholder, and a Midwestern shopping center developer operating in REIT format.

Koger Properties Inc. ($27.00--KOG--NYSE) retains A Rank. This Jacksonville-based investment builder develops suburban, mid-rise campus-type office parks in 27 Sunbelt cities for sale to three related entities: The Koger Co. (KGR--ASE--See REVIEW, July 10); The Koger Partnership, publicly owned (KOG owns 20.1%); and Koger Office Parks, subsidiary formed to build ten new office parks for sale to pension plans managed by Morgan Guaranty Trust Co., New York City. KOG has elected to continue an aggressive construction program in face of soft office markets, adding a bit to market risk.

<u>EPS/CFS/Dividends</u> <u>(Mar. years)</u>:

	1986A	1987A	1988E	3 Yr.%
EPS.....	$0.59	$0.51	$0.50	-7.9%
CFS.....	$2.56	$2.44	$2.50	-1.2%
Dividend.	$2.45	$2.575	$2.60	+3.0%

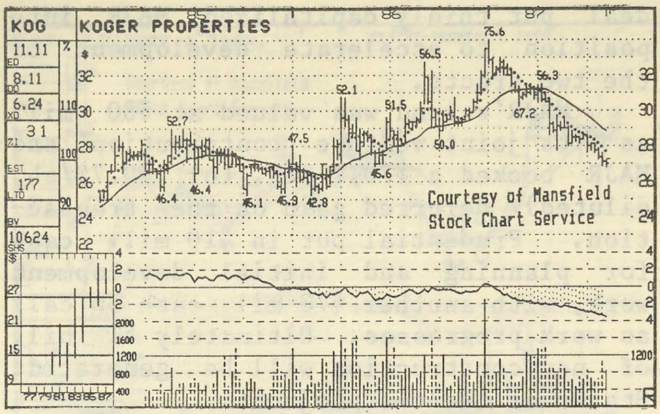
EPS and cash flow per share above include both operating earnings and gains on property sales to related entities, totaling about 45% of total CFS in 1987. KOG earned 2¢ per sh. in the June

qtr. and operating rental CFS of 35¢ was down 12.5%; there were no property sales in either quarter. KOG expects to sell several buildings to related entities during FY 1988, the number depending upon completion and leaseup of inventory properties. Dividends were approx. 80% tax protected in 1987.

Assets and Operations: KOG is building 1.15 mil. sq. ft. of office space in 15 buildings for eventual sale to related entities when they have reached 90% minimum leaseup. KOG holds 54 buildings with about 2.2 mil. SF of space in inventory for sale to KGR and the Morgan accounts. Operating buildings were 84% leased at June 30, reflecting sale of 9 fully leased buildings in FY 1987 and completion of four new buildings this year. (Koger Co. and Koger Partnership buildings are 97% and 100% leased respectively.) KOG builds prototype buildings of 50-100,000 SF in its own office parks. Land for new centers was bought in Memphis (first building opened in May), Orlando, Columbia, S.C. and the Little Rock center expanded. KOG holds 415 acres for expansion.

Financial Measures: Total debt of $168 mil. at June 30 is 1.7 times $100.4 mil. shareholders equity, or $8.52/sh. plus $1.86/sh. accumulated depreciation. Unlike Koger Co., KOG does not provide current appraised value of inventory properties. Debt includes $65 mil. loaned by Koger Co. and the Partnership in advance of property sales. While leverage based on cost appears high, KOG believes its operating methods add value: it builds many copies of smaller prototype buildings in many office parks and produces space at about 65% of competitors' cost. Properties are sold to affiliates at appraised values, typically much higher than cost. KOG's liquidity thus rests on (a) its ability to lease properties profitably, and (b) liquidity of affiliates, currently high.

Exposure: KOG has maintained high occupancies in competitive suburban office markets by keeping tight cost controls, building efficient and repetitive designs, and aggressive leasing of space for 3-5 years to a mix of smaller tenants plus sales offices of major national companies, at rents it believes are 85%-90% of competitive rates. Market exposure is limited by building many small structures in several cities. Cash flow has flattened in recent years and may do so another year or two, causing recent stock price declines. KOG's strategy has worked thru previous cycles and we expect it to work this time.



Major Realty Corp. ($12.25--MAJR--OTC) holds C Rank. We continue to hold it in the Community Builder/Land category of our Portfolio Selector. Over the years several investors have made runs at the stock, most recently accumulation of an 8.4% block by Randon A. Samelson, Bloomfield Hills, Mich. realty operator. Samelson is seeking three board seats and wants to search for a new president.

EPS/Dividends (Dec. years):

	1985A	1986A	1987E	3 Yr.%
EPS.....	$0.10	d$0.67	$0.50	NM
Dividend.	None	None	None	NM

MAJR earned 63¢ and 53¢ per sh. fully diluted in the three and six mon. to June 30, with the June gains coming from sale of a 27.3 acre residential site at Florida Center between Orlando and Walt Disney World. The Sept. qtr. will benefit by about $11 mil. or $1.80-/sh. pretax from sale of 2.48 acres in downtown Tampa to the city for a convention center site; MAJR received $11.375 mil. cash distribution from this sale.

Assets and Operations: MAJR owns two significant Florida land tracts, one the 927 acre Florida Center at the key intersection of Interstate Rt. 4 and the Florida Turnpike between downtown Orlando and Walt Disney World; and 13 acres in downtown Tampa. In Dec. 1984 MAJR put the Tampa tract and 274 prime commercial acres in Orlando into a joint venture with Prudential Insurance; this

deal put thinly capitalized MAJR into position to accelerate development of the two tracts.

MAJR's land was valued at $80 mil. as its joint venture contribution and MAJR booked a $70.7 mil. (or $9.79/sh. diluted) deferred gain on the transaction. Prudential put in $10 mil. cash for planning and initial development work, with another $70 mil. cash on call as work progresses. Ultimately $1 bil. of new construction will be generated. Status of the two projects:

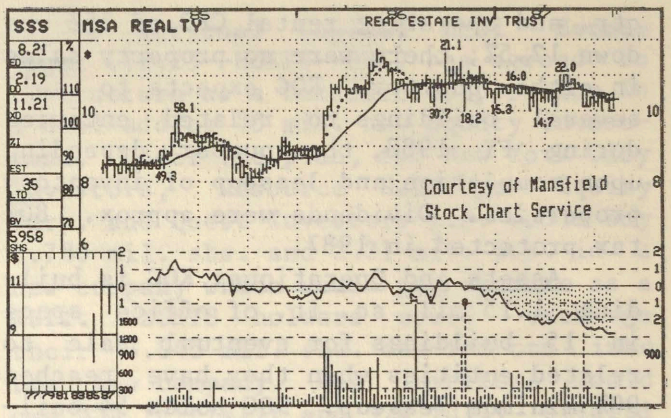
Tampa: The recent land sale to the city of Tampa (in effect MAJR set a minimum price of about $125 per SF for the land) leaves MAJR with about 10.9 acres. More importantly it lets MAJR fix boundaries and begin detail planning and zoning work on a proposed 550,000 SF office, first phase of a project called Garrison Channel Place. MAJR believes its share of development profit could be over $40 mil. over five years.

Orlando: In the first phase here MAJR plans a 978,000 SF upscale Galleria mall, anchored by three high-fashion stores; 1.9 mil. SF office space; and 1 mil. SF hotels and restaurant. The Galleria mall is being put together by a well known shopping center developer who'll get an equity share. Ivey's has signed a letter of intent. MCA Inc. plans to build Universal City Florida on an adjoining 414 acre site. MAJR owns another 414 acres at Florida Center.

Obviously there are many market and financing uncertainties in this scenario, but one estimate puts MAJR's potential value in five years at about $25 per share. There are many negatives: Downtown Tampa has absorbed much office space but vacancy rates remain high. In Orlando's Florida Center, 120,000 SF Major Center Plaza is only 44% leased. And Orlando may not have enough upscale retail buyers to support a Galleria.

Financing: Debt of $23.8 mil. at Dec. 1986 was 4.2 times $5.7 mil. equity at cost. Book value was $1.33 per sh. after the June qtr. gains. Using cash from recent sales, MAJR has called $11.-17 mil. of debentures for redemption as of Sept. 1, in effect forcing conversion into 1.24 mil. shs. at $9. Only other debt is $12.6 mil. mortgages.

Exposure: MAJR's landholdings are



clearly very valuable, altho there are many near-term negatives to development. Potential debenture conversion may bring some price weakness, which we'd use as a buying point.

MSA Realty Corp. ($ 9.75--SSS--ASE) is given C Rank in our initial Ranking. Organized in Mar. 1984, SSS has completed three years as the public shopping center vehicle of Mel Simon Assoc., second largest U.S. shopping center owner/operator.

EPS/CFS/Dividends (Dec. years):

	1985A	1986A	1987E	3 Yr.%
EPS.....	($0.35)	$0.71	$0.20	NM
CFS.....	$0.80a	$2.09a	$0.90	NM
Dividend.	$0.84	$0.95	$1.00	+9.1%

a-Earnings before noncash charges.

SSS is 50% joint venture partner with Mel Simon interests in 11 partnerships owning or building 11 shopping centers. SSS funds 100% of hard costs and earns a construction period return while centers are being built; a 9% preferred return from operations; and 50% of income after certain distributions. Income thus consists of interest and construction period return, plus equity in venture income. In 1986, SSS also earned $5.2 mil. or 84¢ per sh. pretax, on sale of Treasury securities.

SSS earned 4¢ in the Mar. qtr. vs. 35¢ including Treasury securities sale gains and taxloss benefits in 1986. Earnings before noncash charges of 16¢ were down. Dividends are $1.00 annually.

Assets and operations: By end of 1986, SSS had opened seven newly built community shopping centers with 2.08 mil. SF; had three more centers with 980,000 SF under construction; and is expanding an enclosed mall bought in

1984 to 870,000 SF. When all are complete, SSS will own 1.8 mil. SF (or 50%) of 11 centers with 3.63 mil. SF. The enclosed mall being renovated is 560,000 SF Crossroads Center in Omaha, where SSS owns a net 388,000 SF (66%). Seven community centers all are in northern Illinois near Chicago, in Burbank, Bloomingdale, Elgin, Joliet, Orland, Rockford, and Waukegan. SSS just bought 294,000 SF White Oaks centers in Springfield, Ill., and began building 320,000 SF Charles Towne Plaza in St. Charles, Md. (a community being developed by Interstate General L.P.) and 210,000 SF Northland Plaza in Columbus, O.

Financial Measures: SSS is capitalized with low-coupon 9.25% debentures that can be used at par to exercise warrants. Only $20.5 mil of the original $75 mil. debentures remain out and heavy redemptions means most dilution will be worked thru soon. In Jan. SSS refinanced $50 mil. of a planned $150 mil. refinancing of newer centers and reinvested funds in the three recent acquisitions. Debt of $20.5 mil. (all converts) is 0.27 times shareholders' equity of $77.1 mil. Fully diluted book value is $9.01 per share.

Exposure: By focusing on Midwestern markets, SSS hopes to obtain stable retailing growth in solid metropolitan markets, where shopping centers are competitive but not overbuilt. It took advantage of lower interest rates to refinance properties. Shs. have longer-term merit and yield 10%.

RANKING REVIEWS: TWO BUILDER DEVELOPERS WORTH CONSIDERING EVEN IN TODAY'S MARKET

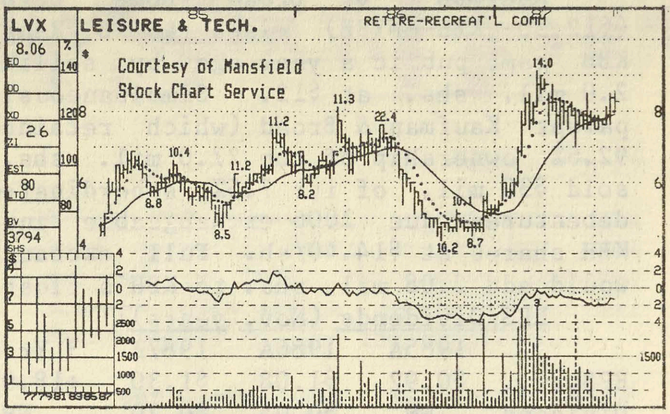
Leisure & Technology Corp. ($9.00--LVX--ASE) continues at C Rank. This adult community builder operates in Calif., N.J. and N.Y., and is entering lifecare centers.

EPS/Dividends (Mar. years):

	1986A	1987A	1988E	3 Yr.%
EPS.....	$0.31	$0.87a	$1.10	+88%
Dividend.	None	None	None	NM

a-Before 66¢ debt retirement loss.

Operating EPS jumped 180% in 1987 on a 55% revenue rise to $137 mil. Land sales, relied upon in some past years, declined sharply. Gross profit margin on $130.4 mil. home sales rose to 21.7%,



major improvement from 9.6%. June qtr. fully-diluted EPS rose 47% to 22¢ on a 78% revenue jump to $35 mil.

Assets and Operations: LVX delivered 933 homes in FY 1987, up 54% from a 1986 hurt by foundation delays for a new Encore model line at its Lakewood, N.J. community. Deliveries were 68% N.J.; 19% Calif.; 12% N.Y. (Long Island); and 2% Fla. Average selling prices rose 18% to $139,800, reflecting success of the Encore line. Backlog of $66.8 mil. in early Aug. was down 2%. LVX holds significant land with approx. 5,000 units planned in present communities (65% N.J.), and just acquired 228 acres on Long Island for 1,000 single-families. It also owns 4,100 acres in N.J.'s restricted Pinelands.

LVX's LeisureCare unit has begun a 307-DU congregate care facility in Lakewood, N.J. and recently joined Ogden Corp. to develop additional facilities.

Financial Measures: A year ago LVX sold $25.5 mil. of 13.38% notes and 996,000 shs. of 9% preferred convertible at $6.40/sh. to repay short-term debt and provide funds to develop some of its considerable land holdings. LVX historically has built good product in good locations but tight cash flow had forced it to sell some land assets to repay debt, limiting longer term potential. Debt of $91.3 mil. is 2.0 times $45.6 mil. common and pfd. equity. Fully converted book value is $5.82/sh.

Exposure - C: Last year's offering has stabilized finances and appears to let LVX maximize future earnings. We see LVX as the preferred play in the hot N.J./N.Y. and retirement markets. The ASE listed preferred ($35.00) sells at conversion parity and yields 6.4%.

Kaufman & Broad Home Corp. ($12.50--KBH--NYSE) rises to B Rank. KBH came public a year ago by selling 2.0 mil. shs. at $12. Simultaneously parent Kaufman & Broad (which retained 92.6% ownership of the 27.0 mil. shs.) sold $30 mil. of its 7.5% subordinated debentures due 2006 exchangeable into KBH shares at $14.40/sh. Full exchange would add 2.08 mil. shs. to KBH's float.

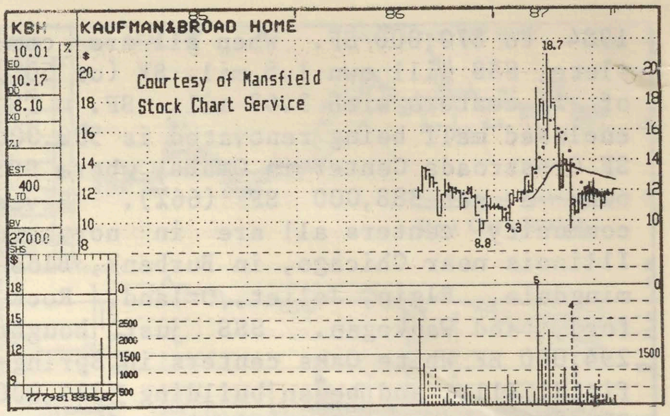
EPS/Dividends (Nov. years):

	1985A	1986A	1987E	3 Yr.%
EPS.....	$0.92	$1.08	$1.30	+18.9%
Dividend.	NM	$0.05	$0.20	NM

KBH earnings quality improved for 1986 and came primarily from housing and land sales. KBH's mortgage banking subsidiary, International Mtg. Co., generated $4.8 mil. pretax income, down because of sharply lower gains on sale of loan servicing rights. KBH earned 41¢ per sh. in the six months thru May, up 46%, on a 57% revenue increase. Dividends are being paid at 20¢ yearly.

Assets and Operations: KBH focuses upon being a strong regional builder and believes its 2% market share in Calif. makes it that state's largest builder. It also builds in Paris, France, only U.S. builder to do so. KBH delivered 4,327 homes in 1986, up 31%, derived 58% Calif., 37% France, 5% in phasing-out Canada. KBH focuses on first time buyers in Calif. Deliveries rose 27% to 1,827 in the half year to May 1987, with Calif. at 66% of deliveries. May backlog of $220 mil. is up. At Nov. 1986 KBH controlled 16,948 lots, about 75% Calif., and has 2,174 acres optioned.

French operations: Your editor recently joined other analysts on a company tour of French operations and found that K&B France is emerging as a significant investment builder as well as France's third largest homebuilder. Most exciting is KBH's entry into retirement housing, which is enjoying strong demand in France. KBH also won hot competition to build a 675,000 SF office complex at Montparnasse in Paris. In housing, KBH builds in both high- and moderate-priced markets, the latter thru subsidiary Bati-Service. All this helps insulate KB France from cyclical swings.



Financial Measures: Debt of $139.3 mil. is 0.87 times equity of $160.6 mil. equity ($5.95/sh. including 24¢ goodwill). KB plans to maintain at least an 80% ownership in KBH, so it can consolidate KBH results for tax purposes, and holds an option to buy 2.75 mil. shs. to maintain this ownership.

Exposure - C: KBH has a long history of developing highly competitive product, and expansion into income properties in France is a big plus.

COMPARATIVE REALTY STOCK GROUP AVERAGE 08/11/87

GROUP NUMBER & NAME	DIV	NON-DIV	TOTAL	SHARE (000)	BOOK VALUE	ANNUAL DIV	EARN ANN	LAST PRICE	-% CHANGE FROM JUL 21	JAN 1	P/E RATIO	ANNUAL YIELD	% PR TO BK	RETURN ON BK	MARKET VAL(000)
1 PROPERTY REITS	55	4	59	6772	10.86	1.09	1.09	14.69	-1.6	-0.7	13.4	7.4	35.3	10.1	6509.7
2 PROP & MTG COMB REITS	22	3	25	5997	12.98	1.37	1.03	13.73	-0.6	-6.7	13.3	10.0	5.8	7.9	2134.8
3 MORTGAGE REITS	17	1	18	5668	13.99	1.82	1.54	14.17	-0.6	-6.1	9.2	12.8	1.3	11.0	1519.0
4 PARTICIPATING MTG REITS	13	0	13	8587	11.45	1.06	0.94	10.47	-0.2	-15.2	11.1	10.1	-8.5	8.2	1387.0
5 MAJOR HOMEBUILDERS	8	4	12	21178	9.25	0.30	1.14	14.34	3.0	4.2	12.6	2.1	55.2	12.3	3152.1
6 OTHER BLDRS/DEVELOPERS	5	29	34	6568	5.07	0.13	0.27	8.21	1.8	10.8	30.2	1.5	61.8	5.4	1990.9
7 INCOME PROP BLDR/OWNR	23	12	35	7687	11.25	0.89	0.91	16.25	0.8	2.9	17.9	5.5	44.5	8.1	4172.8
8 MORTGAGE BANKER/FINANCE	13	4	17	13764	10.32	0.86	1.15	14.50	2.6	-2.0	12.6	5.9	40.5	11.1	5788.8
9 DIVERSFIED RLTY&HOLDING	13	6	19	18799	15.22	0.34	1.32	19.86	4.2	25.7	15.1	1.7	30.5	8.7	12308.5
10 RLTY SVCS/SYNDICATORS	1	7	8	7827	5.34	0.02	0.39	10.45	1.2	21.6	26.9	0.2	95.7	7.3	619.3
11 MANUFACTURED HOUSING	4	6	10	8887	6.72	0.15	0.32	10.54	8.7	5.6	32.9	1.4	56.8	4.8	1355.1
L LIQUIDATING COMPANIES	1	1	2	4719	5.22	0.38	-0.19	5.88	1.1	1.1	NC	NC	12.7	NC	47.3
P PREFERRED STOCKS	1	0	1	1650	10.00	1.10	0.00	13.75	4.8	13.4	NC	NC	37.5	NC	22.7
OVERALL AVERAGE			253	9009	10.47	0.83	0.94	13.74	0.8	2.5	14.6	6.0	31.2	7.9	41008.1
DOW JONES INDUSTRIALS							126.49	2680.48	8.6	41.4	21.2	2.5			
STANDARD & POOR'S 500							15.32	333.33	8.0	37.6	21.8	2.7			
DOW JONES UTILITIES							13.85	210.76	5.0	2.3	15.2	7.6			